

United States Bankruptcy Court
Eastern District of Michigan
Southern Division

In re:

Michael G. Mitchell,
Debtor.

Case No. 04-62654-R
Chapter 7

_____/

Mark H. Shapiro, Trustee,
Plaintiff,

v.

Adv. No. 05-4010

Michael G. Mitchell and Karen J. Mitchell,
Defendants.

_____/

Opinion Regarding Cross-Motions for Summary Judgment

This matter is before the Court on cross-motions for summary judgment on the trustee's adversary complaint seeking to avoid the debtor's transfer of property to himself and his wife as tenants by the entireties.

I.

On March 30, 2003, the debtor purchased property located at 49160 Arlington Ct., Shelby Twp. MI. The purchase price was \$158,000. The debtor financed the purchase with a mortgage in the amount of \$100,000. Almost one year later, on March 5, 2004, the debtor quit claimed his interest in the property from himself to himself and his wife as tenants by the entireties. On August 11, 2004, the debtor filed for chapter 7 relief.

The trustee filed this adversary complaint to avoid the transfer. In Count I, the trustee alleges that the transfer was fraudulent under M.C.L. § 566.34(1)(a) because it was done with the actual

intent to hinder and delay creditors, and under M.C.L. § 566.35 and 11 U.S.C. § 548(a)(1) because the transfer was for less than reasonably equivalent value and was made while the debtor was insolvent. Alternatively, in Count II, the trustee alleges that the transfer was preferential under § 547(b).

The Mitchells assert that the debtor did not transfer an interest in property because at the time, the property was imposed with a constructive trust in favor of Mrs. Mitchell.

The Court concludes that the transfer is a fraudulent conveyance and that the trustee is entitled to judgment. In light of that result, it is not necessary to address the trustee's preference claim.

II.

In support of his motion for summary judgment, the trustee contends that the transfer is avoidable as a fraudulent conveyance under 11 U.S.C. § 548(a)(1)(B) and M.C.L. § 566.35 because the debtor received less than reasonably equivalent value in exchange for the transfer and the debtor was insolvent at the time the transfer was made.

In response to the Mitchells' argument that the Court should impose a constructive trust, the trustee contends that such a remedy is limited to situations where either a trust was imposed by a court judgment pre-petition or, upon relief from the automatic stay, a state court judgment is entered imposing a constructive trust and the property is not subject to distribution to creditors. The trustee asserts that because there was no pre-petition action initiated by Mrs. Mitchell to determine her interest in the property, the Court cannot impose a constructive trust. Further, the trustee contends, imposing a trust would affect the ratable distribution to creditors, resulting in no distribution from the property.

The Mitchells assert because the home was subject to a constructive trust in favor of Mrs. Mitchell, Mr. Mitchell did not transfer his interest in the property. The Mitchells state that they have been married for 40 years and have owned four homes during that time. With the exception of the home at issue, they state that each of these homes have been held as tenants by the entireties at all times. They contend that they purchased the property at issue using the proceeds from the sale of their prior home as a down payment. They assert that at the time they purchased the home, they were having financial difficulties. They contend that the home was purchased in the name of Mr. Mitchell only so that they could obtain a more favorable mortgage terms. They argue that it was their understanding and intent that the deed would be immediately transferred by Mr. Mitchell to both as tenants by the entireties. They (mistakenly) stated in their affidavit that Mr. Mitchell signed a quit claim deed at the time of the closing, however, the title company never recorded it. They contend that they did not discover that the deed was never recorded until March 2004, at which time they immediately prepared and recorded a new quit claim deed. Mrs. Mitchell contends that in addition to contributing half of the down payment, she has shared equally in the monthly mortgage payments and the expenses for the home. The Mitchells argue that the transfer was not done with the intent to hinder, delay or defraud creditors.

The Mitchells submitted a supplemental response which included an affidavit of Judy Gottage from their mortgage company. She states that the quit claim deed was prepared and presented at the time of closing. However, it was not signed by Mr. Mitchell. She states that she did not discover that it had not been signed or filed until March, 2004, when she was contacted by the Mitchells, who were requesting a copy of the quit claim deed.

III.

As noted, the Mitchells assert that there was no transfer of an interest of the debtor in property because the property was held in trust for the debtor's wife.

The party seeking imposition of a constructive trust bears the burden of establishing the trust requirements. *U.S. Dept. of Energy v. Seneca Oil (In re Seneca Oil)*, 906 F.2d 1445, 1449 (10th Cir. 1990). State law determines the interests of the parties in the property at issue. *Unsecured Creditors' Comm. of Highland Superstores, Inc. v. Strobeck Real Estate, Inc. (In re Highland Superstores, Inc.)*, 154 F.3d 573, 578 (6th Cir. 1998) (citing *Butner v. United States*, 440 U.S. 48, 54, 99 S. Ct. 914 (1979)); *Demczyk v. Mut. Life Ins. Co. of N.Y. (In re Graham Square, Inc.)*, 126 F.3d 823, 827 (6th Cir. 1997).

With regard to a constructive trust, the Sixth Circuit held in *XL/Datacomp, Inc. v. Wilson (In re Omegas Group, Inc.)*, 16 F.3d 1443 (6th Cir. 1994), that a constructive trust cannot be imposed by the bankruptcy court. The court stated, "Because a constructive trust, unlike an express trust, is a remedy, it does not exist until a plaintiff obtains a judicial decision finding him to be entitled to a judgment 'impressing' defendant's property or assets with a constructive trust." *Omegas Group*, 16 F.3d at 1451. The court also stressed that the imposition of a constructive trust in that case would have undermined the Bankruptcy Code's goal of equitable distribution. *Id.* at 1452-53.

In *McCafferty v. McCafferty (In re McCafferty)*, 96 F.3d 192 (6th Cir. 1996), the Sixth Circuit recognized that imposition of a constructive trust might be appropriate when property in bankruptcy was not subject to distribution to creditors and therefore did not implicate the rationale of ratable distribution.

Finally, in *Poss v. Morris (In re Morris)*, 260 F.3d 654 (6th Cir. 2001), the Sixth Circuit further limited its previous holding in *In re Omegas Group, Inc.*, by establishing the rule that no prior judicial determination is needed when state law recognizes, as a matter of law, the existence of a prepetition constructive trust. *Id.* at 666.

Under Michigan law, a constructive trust may be imposed “where such trust is necessary to do equity or to prevent unjust enrichment[.]” *Ooley v. Collins*, 73 N.W.2d 464, 469 (Mich. 1955). Such a trust may be imposed when property ““has been obtained through fraud, misrepresentation, concealment, undue influence, duress, taking advantage of one’s weakness, or necessities, or any other similar circumstances which render it unconscionable for the holder of the legal title to retain and enjoy the property[.]”” *Potter v. Lindsay*, 60 N.W.2d 133, 136 (Mich. 1953) (quoting *Racho v. Beach*, 236 N.W. 875, 877 (Mich. 1931)).

The Mitchells rely on *McCreary v. Shields*, 52 N.W.2d 853 (Mich. 1952), and *Kent v. Klein*, 91 N.W.2d 11 (Mich. 1958), in support of their position that Michigan law would impose a constructive trust on the property in favor of Mrs. Mitchell. In *McCreary*, the plaintiff and her husband purchased property (Lot K) pursuant to a deed which mistakenly described the adjacent vacant parcel (Lot L). The plaintiff and her husband resided in the house on Lot K, but mistakenly paid the taxes on Lot L. Due to the delinquent tax status of Lot K, the state received title to Lot K through delinquency proceedings and conveyed the property to the defendant for \$150. The defendant admitted that she believed she had purchased a vacant lot, and the state had not attempted to collect rent from the plaintiffs. The trial court awarded Lot K to the plaintiff. In affirming, the Michigan Supreme Court stated, “[d]efendant [] has no just ground for complaint that she is not allowed to unjustly enrich herself out of the error common to all three parties[.]” “ *McCreary*, 52

N.W.2d at 855. The court concluded that a constructive trust was a proper remedy to prevent the defendant's unjust enrichment. *Id.*

In *Kent*, title to a parcel of real estate was conveyed by deed to the defendant to hold in trust for her incompetent brother. After the death of the defendant's brother, the brother's widow and son sued for delivery of legal title to them. The defendant refused to transfer title to the property because legal title was in her name. The court upheld the trial court's decision to establish a constructive trust, finding that the property was unconscionably withheld. *Kent*, 91 N.W.2d at 14-15.

The circumstances here are very different from those where Michigan law has recognized a constructive trust. Here, taking the Mitchells' assertions of fact as true, the debtor and his wife had a secret arrangement to take title in the debtor's name and then transfer it to the debtor and his wife. The debtor has in no way obtained this property through fraud, misrepresentation, concealment, undue influence, or duress. He did not take advantage of any necessity or weakness on his wife's part. She was a full participant in the plan to put the property in the debtor's name, and their failure to carry out the balance of their plan, assuming there was such a plan, does not render his title unconscionable nor his estate unjustly enriched. To the contrary, the constructive trust that the Mitchells seek will unjustly shield the property from creditors and violate the Sixth Circuit's holding that secret trusts should not be enforced when they affect the equality of distribution. *XL/Datacomp, Inc. v. Wilson (In re Omegas Group, Inc.)*, 16 F.3d 1443 (6th Cir. 1994).

The Court concludes that the Mitchells have failed to establish that Michigan law would recognize a constructive trust as a matter of law, and that therefore, the deed at issue did transfer the property from the debtor to the defendants.

IV.

In order to avoid a transfer under 11 U.S.C. § 548(a)(1)(B), the court must determine both that the debtor received less than reasonably equivalent value for the transfer and that the debtor was insolvent at the time of the transaction or was rendered insolvent by the transaction. *Lim v. Greenfield (In re Greenfield)*, 249 B.R. 856, 858 (Bankr. E.D. Mich. 2000), *aff'd*, 65 Fed. Appx. 549 (6th Cir. 2003).

Similarly, M.C.L. § 566.35 provides:

(1) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made or the obligation was incurred if the debtor made the transfer or incurred the obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation.

M.C.L. § 566.35(1).

The trustee bears the burden of proving the elements of a fraudulent conveyance by a preponderance of the evidence. *Lisle v. John Wiley & Sons, Inc. (In re Wilkinson)*, 319 B.R. 134 (Bankr. E.D. Ky. 2004).

The Mitchells do not dispute that the debtor was insolvent at the time of the transfer.

However, the Mitchells do argue that the debtor received reasonably equivalent value in exchange for the transfer because Mrs. Mitchell contributed half of the down payment and contributed to the household expenses.

A transfer on account of an antecedent debt can constitute fair consideration. *Pereira v. Dow Chemical Co. (In re Trace Int'l Holdings, Inc.)*, 301 B.R. 801, 805 (Bankr. S.D.N.Y. 2003).

“[E]quivalent value may be the satisfaction of an antecedent debt of the Debtor.” *Pummill v. Ameristeel, Inc. (In re Richards & Conover Steel, Co.)*, 267 B.R. 602, 613 (B.A.P. 8th Cir. 2001).

In *Rubin v. Manufacturers Hanover Trust Co.*, 661 F.2d 979, 991 (2d Cir. 1981), the court explained that if the debtor receives property or discharges an antecedent debt that is substantially equivalent in value to the property given by him in exchange, then the transaction has not significantly affected his estate and his creditors have no cause to complain. However, if the benefit of the transaction to the debtor does not substantially offset its cost to him, then his creditors have suffered.

One half of the down payment amounted to \$30,875. However, nothing in the record suggests how much money Mrs. Mitchell contributed to the household expenses and the Mitchells have provided no documentation of that.

The trustee states that the debtor has \$60,000 in equity in the home. Prior to the transfer, creditors would have been entitled to some distribution from the proceeds from the sale of the home. After the transfer, Mrs. Mitchell holds an undivided half interest in the home, from which the creditors would be entitled to nothing.

Therefore, the Court concludes that the record establishes that the debtor did not receive reasonably equivalent value in exchange for the transfer.

Further, “[t]he Michigan Supreme Court ‘has consistently held that during insolvency entireties estates cannot be created or enhanced at the expense of creditors and that relief may be granted without reference to any actual fraudulent intent.’ *Glazer v. Beer*, 343 Mich. 495, 498, 72 N.W.2d 141 (1955). *See also Craft v. United States*, 65 F. Supp.2d 651, 658-59 (W.D. Mich. 1999); *Hoerner v. Elkins (In re Elkins)*, 94 B.R. 932, 934 (Bankr. W.D. Mich. 1988) (Entireties estates

cannot be created at the expense of creditors.).” *Greenfield*, 249 B.R. at 859.

Accordingly, the transfer is avoidable under 11 U.S.C. § 548(a)(1)(B) and M.C.L. § 566.35.

The Court will enter an appropriate order.

_____/s/_____
Steven Rhodes
Chief Bankruptcy Judge

Entered: July 27, 2005

cc: Nicole C. Amey
Tracy M. Clark

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